

GASB STATEMENT 34 IMPLEMENTATION PROCEDURES

Elimination of Internal Activities and Balances

Background

GASB 34 requires that internal activity and balances reported as interfund activity in fund financial statements be reclassified or eliminated in the preparation of the government-wide statements of net assets and activities. This elimination will avoid the "grossing up" of amounts resulting from internal activity within the primary government.

Interfund Activity

Activity that takes place between and among governmental, proprietary, and fiduciary funds, as well as blended component units, in the fund financial statements, such as transfers and their associated due to's and due from's, and revenues and expenses/expenditures with their associated receivables and payables, is called Interfund Activity. This interfund activity within the fund statements will have to be analyzed and reclassified and/or eliminated in the government-wide statement of net assets and statement of activities. This interfund activity reported in the fund statements could be either reciprocal or nonreciprocal.

Reciprocal interfund activity is the internal counterpart to exchange and exchange-like transactions, and includes interfund loans and interfund services provided and used. Reciprocal interfund activity generally should be reported as revenues and expenses or expenditures in the fund operating statements and as receivables and payables in the fund balance sheets.

- (1) *Interfund loans* are amounts provided between funds with a requirement for repayment. These amounts should be reported as receivables and payables, and should not be reported as Other Financing Sources in the fund statements. However, if repayment is not expected in a reasonable amount of time, then the amount that is not expected to be repaid should be reported as a transfer from the fund that made the loan to the fund that received the loan. Whether the loan is eventually reclassified as a transfer or not, these amounts will be eliminated in the government-wide statements as discussed below under internal balances and internal activity.
- (2) *Interfund services provided and used* are sales and purchases of goods and services between funds for a price approximating their external exchange value. If the government, for the purposes of economy or efficiency, uses the general fund to purchase supplies for other funds, and spreads the cost to these other funds based on a usage criteria, then this type of transaction is not interfund services provided and used, because the purchase and resale of office supplies is not a program of the general fund. Instead, an example of an interfund service provided and used type of transaction would be the sale of water from the water

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fund (an enterprise fund) to the general fund. These transactions are not an allocation of costs between funds in a government, but are instead the purchase and sale of something that the government must have to function properly, and are in effect, arm's length transactions. These transactions should be presented in the fund statements as revenues and expenses/expenditures and receivables/payables. These revenues and expenses should not be eliminated in the statement of activities if they occur between functions. They may be eliminated if they occur within functions, but are not required to be unless the effect on direct expenses or program revenues is material. Receivables and payables associated with revenues and expenses between functions should also not be eliminated in the statement of net assets.

Nonreciprocal internal activity is the internal counterpart to nonexchange transactions, including interfund transfers and interfund reimbursements.

- (1) *Interfund Transfers* are the flow of assets from one fund to another fund without the equivalent flow of assets in return, and without a requirement for repayment. Transfers are reported as other financing sources or uses in the fund statements, and amounts not transferred but obligated at year end are reported as due to's and due from's in the fund statements. Transfers and due's within governmental activities and within business-type activities should be eliminated in the Statement of Net Assets and the Statement of Activities; however, the net amount transferred or due between governmental and business-type activities should be reported. This amount should be called "Internal Balances" on the Statement of Net Assets and "Internal Activity" on the Statement of Activities, and will zero out in the total primary government column. Internal Balances and Internal Activity will also include any interfund loans, but not interfund services provided and used.
- (2) *Interfund Reimbursements* are repayments to funds who initially paid an expenditure or expense from the funds ultimately responsible for them. Reimbursements should not be displayed in the financial statements, meaning that the "revenue" of the fund receiving the reimbursement should not be shown in the financial statements. Instead, an expenditure or expense, as appropriate, should be recorded in the reimbursing fund, and a reduction in an expenditure or expense should be recorded in the fund that is reimbursed. In this way the expenditure or expense is not recorded twice in the financial statements.

Intra-Entity Balances

GASB 34, paragraph 58 (see enclosure B, p. 5) states that any amounts due to or due from the primary government from or to fiduciary funds in the fund statements would be shown as receivables from and payables to external parties in the government-wide Statement of Net Assets, and would not be included in the internal receivables and

payables amount (internal balances). GASB believes that these transactions are between the primary government and beneficiaries or other external parties, instead of between the primary government and the fiduciary funds themselves. GASB 34 does not specifically mention transfers between the primary government and fiduciary funds; however, we feel that any such transfers in the fund statements should be reclassified as revenues (could be shown as either a capital or operating grant, or general revenue, as appropriate) or expenses under governmental activities in the Statement of Activities. This would be in line with GASB's requirement that any due to's and due from's between the primary government and fiduciary funds in the fund statements would be shown as receivables from and payables to external parties in the government-wide Statement of Net Assets. The state had transfers from the general fund to three of the retirement systems for fiscal year 1999.

Interfund activity does not include transactions between the primary government and its discretely presented component units. These transactions will be considered as transactions with external parties, and should be reported as revenues and expenditures/expenses in both the fund statements and the government-wide statements. However, any associated receivables and payables should not be grouped in with other receivables and payables, but instead should be displayed on a separate line, such as "Receivable from the state" or "Payable to component units". The total receivables and payables between the primary government and the discretely presented component units shown in the fund statements can be netted in the government-wide statement of net assets.

In the Sample State Government Financial Statements shown in the GASB 34 Implementation Guide, amounts are shown as receivables and payables between the primary government and its discretely presented component units in the sample state government combining balance sheet for governmental funds. However, in the government-wide statement of net assets, the total receivable and payable amounts are netted, and this net amount is shown as a due to or due from component units (see enclosure A, pp. 4 & 5). In order to clarify this issue, I called GASB. Ken Shermann from GASB stated that the terms receivables/payables and due to's/due from's can be used interchangeably on either the fund statements or the government-wide statements. He said that GASB didn't want to use the same term for both the fund statement and the government-wide statement in the sample state government because then it would appear that whichever way they used, that that way would be the only way to do it.

However, we feel that due to's and due from's should be used in the fund statements when they are associated with transfers between funds within the primary government and blended component units not including fiduciary funds, **not** as a synonym for receivables and payables to be used whenever a different word is desired. GASB 34, paragraph 61 (see enclosure B, p. 5) states that

"resource flows (except those that affect the balance sheet only, such as loans and repayments) between a primary government and its discretely presented component units should be reported as if they were external transactions -that is, as revenues and expenses. However, amounts payable and receivable between the primary government and its discretely

presented component units or between those component units should be reported on a separate line.”

We feel that they should be shown as receivables and payables in the government-wide statement of net assets, instead of due to's and due from's, as calling these amounts receivables and payables in the fund statement and calling the same amounts due to's and due from's in the government-wide statement could be confusing to financial statement users.

Internal Balances

GASB 34 defines **Internal Balances** as the net residual amounts due between governmental and business-type activities in the government-wide Statement of Net Assets. The amounts that will be shown as internal balances will be the interfund receivables and payables and the Due To's and Due From's that take place between governmental activities and business-type activities of the primary government. Any Interfund receivables and payables and due to's and due from's that are within governmental activities or within business-type activities will have to be eliminated on the Statement of Net Assets. The remaining amounts due between governmental and business-type activities will be the Internal Balances amount.

This amount can be shown as a positive and a negative in either the asset or liability section of the Statement of Net Assets, depending on whether the net Internal Balances are from business-type activities to governmental activities (would be shown in the asset section), or to business-type activities from governmental activities (would be shown in the liability section). Using this presentation, the positive and negative amounts would zero out in the Total Primary Government column of the Statement of Net Assets in either the asset or the liability section (see enclosure A, p. 1).

Alternately, the internal balances could be reported separately in the asset and liability sections as internal receivables and internal payables and then adjusted out of the total primary government column. In other words, the total primary government column would show zero for internal receivables and internal payables, even though amounts were shown that didn't add up to zero. If this approach is taken, a notation would have to be made on the face of the statement that internal receivables and payables have been eliminated from the total column. A problem with this method of presentation is that the statement will not foot across (enclosure A, p. 2). Therefore, we feel that the method of display showing a positive **and** a negative amount in **either** the asset **or** the liability section is preferable for Louisiana.

Internal Activities

The effect of internal service fund activity will have to be eliminated for the statement of activities. Internal service fund activity is doubled in the fund financial statements because a revenue and an expense are shown in the internal service fund and an

expense or expenditure is also shown in the fund that the internal service fund provided service to.

Eliminating the effect of internal service fund activity in the government-wide statement of activities involves two steps: first, the internal service fund revenues and expenses are reported in the proprietary fund statement, but **not** in the statement of activities, and second, any profit or loss reported by the internal service funds will have to be allocated back to the funds or agencies that the internal service funds provided services to. This allocation will cause the internal service funds to break even, and not show either a profit or a loss. The effect of similar internal events that are basically allocations of overhead expenses from one function to another or within the same function also should be eliminated, so that the allocated expenses are reported only by the function to which they were allocated. Procedures to remove the effects of internal service funds and similar internal events will be addressed in a separate procedure paper.

Suggested Procedure

In order to accommodate the eliminations of internal balances and internal activities between funds within both the governmental and business-type activities columns, to reclassify the due to's and due from's and transfers between the fiduciary funds and the primary government to external receivables/payables and revenues/expenses, and to identify the receivables/payables as well as revenues and expenditures/expenses between the primary government and its component units, we will have to modify our current method of identifying and reporting transfers and other inter-agency transactions.

For interfund loans such as seeds and advancements, amounts will have to be identified, perhaps by a new system account, so that we could see the transactions taking place. These transactions will be shown in the fund statements, but eliminated in the statement of net assets if within governmental and business-type activities, and classified as part of internal balances if between governmental and business-type activities.

For interfund services provided and used, these amounts will not be eliminated from the fund statements, and will be shown as revenues/expenses and receivables/payables in the government-wide statements.

For transfers, we could set up a new report similar to the current infomaker report used for transfers, and identify each transfer and due as either to or from governmental activities, business-type activities, fiduciary funds, or discrete component units. Transfers between the primary government and discretely would be reported as receivables/payables and revenues and expenses/expenditures in both the fund statements and the government-wide statements. Transfers between the primary government and fiduciary funds would be reported as transfers and dues in the fund statements and as receivables/payables and revenues/expenses in the government-wide statements. Transfers and dues within governmental and business-type activities would be eliminated in the government-wide statements. Transfers between

governmental and business-type activities would be presented as internal balances and internal activities.

For reimbursements, in the fund statements an expense or expenditure is recorded in the reimbursing fund, and a reduction of an expense or expenditure is recorded in the fund that is reimbursed. In the government-wide statements, an expense would be recorded in the reimbursing activity (governmental or business-type), and a reduction in an expense would be recorded in the activity that is reimbursed.

The table below shows how the following internal transactions will be presented:

Transaction	Fund Statements	Statement of Net Assets	Statement of Activities
Interfund Loans	Receivables/payables	1. within governmental or business-type activities: eliminate 2. between governmental and business-type activities: present as internal balances	Not applicable
Interfund Services provided and used	Receivables/payables Revenues/expenses or expenditures	1. within governmental or business-type activities: receivables/payables – should not be eliminated 2. between governmental and business-type activities: should not be eliminated	1. within governmental or business-type activities: revenues/expenses – may be eliminated if the effect on direct expenses or program revenues is material 2. between governmental or business-type activities: should not be eliminated
Interfund Transfers	Due to's/Due from's Transfers	1. within governmental or business-type activities: eliminate 2. between governmental and business-type activities: present as internal balances	1. within governmental or business-type activities: eliminate 2. between governmental or business-type activities: present as internal activity
Reimbursements	1. Expenditure/expense in reimbursing fund 2. Reduction of expenditure/expense in fund that is reimbursed	Not applicable	1. Expense in reimbursing entity 2. Reduction of expense in entity that is reimbursed
Transfers between primary government and fiduciary funds	Due to's/Due from's Transfers	Receivables/payables from external parties	Revenues/expenses from external parties
Transfers between primary government and discrete component units	Receivables/payables Revenues/expenses or expenditures	Receivables/payables shown as separate line item (receivable from state, payable to component units)	Revenues/expenses from external parties